MARKET UPDATE

Monthly Market Summary for Members of DFMC

Dairy Farmers Milk Co-operative

June 2010

Woolworths shakes up milk shares

Woolworths changes tack in domestic milk packaging contracts as it gives a slice of business to Parmalat and MG.

NatFoods has lost a part of its 300 million litre house-brand contract to supply private label milk products to Woolworths, following the retailer's decision to award its southern NSW contract to Murray Goulburn and the Queensland and ACT contracts to Parmalat. NatFoods holds onto supply contracts in all other regions, but these new arrangements will be re-tendered again in 2011, increasing the uncertainty for the company and suppliers. The private label supply contract changes take effect in September this year, but the AFD volumes agreed for 2010/11 between DFMC and NatFoods remain in place until July 2011.

The Queensland loss will not reduce the likely demand by NatFoods to meet the private label supply requirements for DFMC "tier 1" milk until July 2011. NatFoods will abide by current AFD volumes with DFMC suppliers and continue to buy the 77 million litres of milk at stake at a "tier 1" price until July 2011, following which farmers would face a change in the demand volume as overall market shares are subject to change in the meantime.

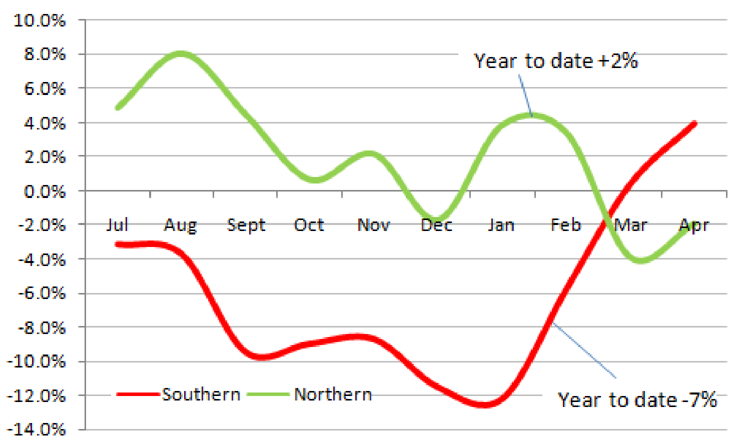
April's milk output improved

The trend of more in the south and less in the north has continued

National milk production was up 2.7% in April 2010 but year to date output for the 10 months of the 2009/10 season remained 5.2% down on the prior year, as the southern region continued to bask in good conditions and producers in northern areas of the industry steadied their milk output.

Strong increases in Gippsland and Western Victoria showed the effect of a good seasonal break, low bought-in feed and optimism about next season milk prices, but the north of Victoria was still deep in reverse due to early season losses of cow numbers. The message about the cost of over-production seems to be getting across in Qld and NSW which each recorded lower milk output than the same period in 2009. Milk production in NSW for the 10 months to April is now just 1.1% ahead of the same time in 2008/09.

Monthly production v same time in the prior year (2009/10)



Retail sales remain sluggish

The "economic recovery" is proving to be a weak one

April retail sales showed the economy was slowing as households pulled back on splashing cash and cards on household durables and took advantage of cheaper offers by major supermarkets and department stores. The latest measure of consumer sentiment (tracked by Westpac) sees consumers again worried about the coming months, but the mood remains considerably brighter than in the period of the GFC.

Important market indicators

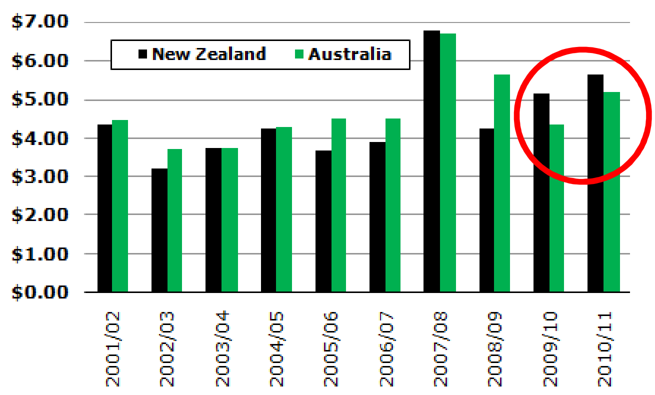
Dairy export index	The index has risen to 157pts , up about 8% on the last month, with the sharp fall in the $A the major benefit
World dairy prices	All spot prices steady, except for SMP which lost US$200 after recent news of EU's stockpile clearance sale
Grain futures	Prices in US have weakened further, whereas Australian futures prices have increased with the weakening in the $A
Cow prices for cull exports to the US	The US market for Aussie cull cows is a weaker with less tension in the US domestic market. The weaker $A hasn't helped prop up $A values

Fonterra opens at $4.36/kg ms

The Australian arm of the NZ co-operative opens lower than expected.

Fonterra Australia has set an opening 2010/11 milk prices in Victoria and Tasmania which will provide a forecast average price of $4.36 per kilogram of milk solids, up 20% from last year's opening. The opening price will be gazumped by others in the coming weeks. The Dairy Australia opening price range of $4.40 to $4.60/kg (38-41cpl) remains the best guess at the 2010/11 season start, although the recent fall in the $A's value may push numbers slightly higher.

Australia vs NZ farmgate milk prices in nominal $A



Big difference in NZ forecast payouts

NZ's major players have forecast 2010/11 milk prices

Fonterra has announced a payout forecast for the full 2010/11 season in New Zealand of $6.90-$7.10/kg MS, which includes a milk price of $6.60/kg MS and a distributable Profit of 30-50c/share. Fonterra Chairman, Henry van der Heyden, said at the time that if prices and the currency stay where they now are for the whole season, a payout of more than $8 is a possibility.

Small South Island manufacturer, Westland Milk Products, meanwhile has announced a "prudent" forecast opening payout of NZ$5.80-$6.20 per kilogram of milk solids for the 2010/11 season.

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World dairy market returns

Prices steady, dollar helps index

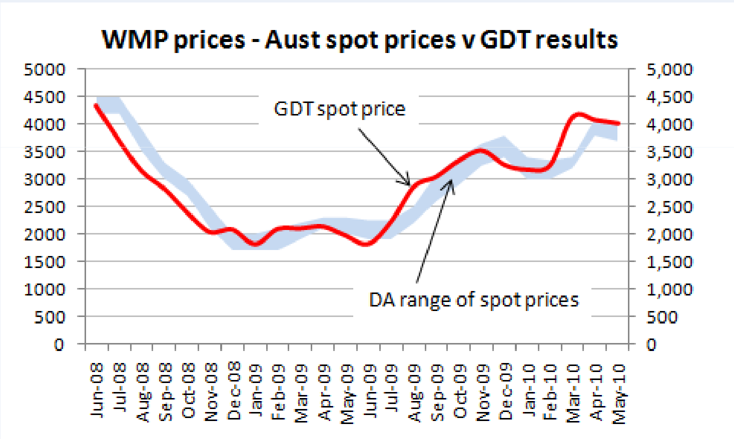
At the time of this report the index of Australian export returns had improved further on last month in net terms by about 12 points over the past few weeks, with slightly weaker spot prices but a sharp fall in the value of the $A.

The value of the $A fell heavily in late May and early June as the financial systems in several European countries pushed currency speculators to hide in the US dollar rather than riskier currencies such as the $A. The worsening outlook for the Chinese economy – and its effect on commodity metals prices – also helped pull the $A down.

GDT auction holds its nerve

Export spot prices remain relatively stable with the only weak spot being SMP as the EU flagged a program to clear some of its stockpile (see below) The average price for WMP again slipped in the GDT auction event in early June. Fonterra reported that the trade weighted index covering the basket of products fell 3.5 per cent.

Whole milk powder average prices were down 3.4 per cent to US$3790 a tonne, while SMP fell 6.2 per cent to an average price of $3462/t. In contrast, anhydrous milkfat posted a rise of 5.9 per cent to $5324/t.



EU sells some of its stockpile

The EU built up large stockpiles of butter and SMP product in 2009 and 2010 when it opened its doors to buying product off the market to assist stabilise prices as the GFC took effect. Intervention buying has long been used as an internal market remedy by the EU to protect its industry from volatility, but the existence of major stockpiles actually adds to greater uncertainty – when will they release them?

With stocks of 260,000 tonnes in SMP and about 76,000 tonne of butter, the EU decided in May to release up to 25,000 tonnes of butter and 65,000 tonnes of skimmed milk powder from these "intervention stocks" in a first round of offers to help clear some of the mountain. This came after intense lobbying by the industry for the EU Commission to release stocks to subdue rising prices and increase market supply.

The first round of these clearances saw a total of 11,551 tonnes of butter sold at prices ranging from €3450 to €3851/tonne (about US$4100 to US$4600/tonne). The commission rejected further bids for 60,930t of butter along with all bids (of 48,999t) for SMP, as the prices offered were deemed too low compared to the present market prices and too far below the market average.

Again this is a sign of the different times we are in, as the Commission has taken a more active role in stabilising markets at prices which are high, but probably sustainable for its EU industry.

Take note: The index is an indicator of spot trends in gross export returns to the industry based on quoted Australasian export prices, movements in currency and the total milk usage in exports by the Australian industry. It was set at 100 on 1 January 2004.

Source: Freshlogic

New futures platforms operating

Two new futures markets are now open for manufacturers and buyers

Two new dairy futures trading operations, one based in Chicago operated by the Chicago Exchange, and a second that opened this week based in Frankfurt operated by Eurex, offer trade for the first time in SMP and butter on the world market. The futures products are based on a number of physical delivery points around the world.

Trading is very quiet to date but the step reminds of the major changes in the world market that have been sufficient for owners of the exchanges to offer the products.

Another US herd retirement plan but milk supply grows

CWT conducts another retirement programme to sustain US milk prices.

The US dairy-farmer owned Cooperatives Working Together (CWT) is conducting its 10th herd retirement program, hoped to give a further push to milk prices in the US. But US milk production is again on the move, showing just how strong the supply of young cattle is in the massive industry.

After reporting a decline of 0.1 per cent in the first quarter of 2010, US milk production has enjoyed an unexpected boost in April, coming in 1.5 per cent up from a year ago, doubling the rate of growth in March and signalling a recovery in production that may dampen wholesale markets. California recorded its first gain in 17 months with a slight growth in production while Wisconsin posted an increase of 6.2 per cent.